United States Environmental Protection Agency

Office of Enforcement and Compliance Assurance

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EPA

The Effect of Superfund on Lenders That Hold Security Interests in Contaminated Property

Office of Site Remediation Enforcement

Quick Reference Fact Sheet

The Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA, commonly known as Superfund) provides a security interest exemption which protects certain lenders from owner/operator liability under CERCLA. In September 1995, EPA and the Department of Justice (DOJ) issued a statement clarifying their enforcement policy with respect to lenders. Designed for use by EPA staff, this fact sheet summarizes CERCLA's security interest exemption and the Policy on CERCLA Enforcement Against Lenders and Government Entities that Acquire Property Involuntarily ("Lender Policy"). This fact sheet also answers common questions about the effect of CERCLA on lenders.

Introduction

The Lender Policy was issued as part of EPA's Brownfields Economic Redevelopment Initiative, a series of efforts designed to help states, communities, and other stakeholders in economic redevelopment to work together in a timely manner to prevent, assess, safely clean up, and sustainably reuse brownfields. Brownfields are abandoned, idled, or under-used industrial and commercial facilities where expansion or redevelopment is complicated by real or perceived environmental contamination. Banks and other lending institutions may hesitate to lend money for brownfields redevelopment and other purposes because they fear that they will incur Superfund liability. This fact sheet summarizes the applicable CERCLA statutory provision and the Lender Policy, and answers common questions about the effect of CERCLA on lenders.

Legal Background

Section 101(20)(A) of CERCLA, 42 U.S.C. § 9601(20)(A), provides an exemption from owner/operator liability for a person who holds evidence of ownership in a CERCLA facility primarily to protect a security interest in that property, provided the person does not participate in the management of the facility. CERCLA does not define "participation in management" or any other key terms used in its security interest exemption.

In 1992, EPA issued the Lender Liability Rule to clarify CERCLA's security interest exemption. See Vol. 57, No. 83 of the Federal Register at pp. 18344 to 18385 (April 29, 1992). The Rule and its preamble defined and provided examples of permissible pre-loan, pre-foreclosure, and post-foreclosure activities for lenders. (The Rule also addressed involuntary acquisitions by government entities, which is the subject of "The Effect of Superfund on Involuntary Acquisitions of Contaminated Property by Government Entities," a fact sheet issued by the Office of Site Remediation Enforcement in December 1995.)

In a 1994 decision that did not criticize the substance of the Lender Liability Rule, the D.C. Court of Appeals vacated the Rule after it determined that EPA did not

have the statutory authority to issue a rule delineating the scope of CERCLA liability. See Kelley v. Environmental Protection Agency, 15 F.3d 1100 (D.C. Cir. 1994).

Lender Policy

In September 1995, EPA and DOJ issued their Lender Policy. The Lender Policy reaffirms that EPA and DOJ will generally follow the approach of the Lender Liability Rule and its preamble when exercising their enforcement discretion to determine whether particular lenders may be subject to CERCLA enforcement actions. The Lender Policy does not restate or summarize the substance of the Rule or preamble, but merely endorses the interpretations and rationales announced in the Rule and its preamble.

Under the Lender Policy, the following principles apply to lenders:

- While the borrower is in possession of the facility, a lender "participates in management" (and therefore does not qualify for CERCLA's security interest exemption) if the lender:
  - ▸ Exercises decision-making control over the borrower's environmental compliance, such that the lender has undertaken responsibility for the borrower's hazardous substance handling or disposal practices; or
  - ▸ Exercises control similar to that of a manager of the borrower's enterprise, such that the lender is involved with day-to-day decision-making related to (1) environmental compliance, or (2) all, or substantially all, of the operational (as opposed to financial or administrative) aspects of the enterprise other than environmental compliance.
- Before the inception of a loan, a lender will not be deemed to "participate in management" if it:
  - ▸ Undertakes or requires an environmental inspection of a facility (although it is not required to do so); or
  - ▸ Requires a prospective borrower to clean up a facility.
- Before foreclosure, a lender can undertake loan "policing" activities without incurring owner/operator liability, provided the lender does not thereby "participate in management" as described above. As a result, a lender can generally:
  - ▸ Require the borrower to clean up the facility;
  - ▸ Require the borrower to comply with environmental laws and regulations or any warranties or covenants; and
  - ▸ Monitor or inspect the facility or the borrower's business or financial condition.
- Before foreclosure, a lender can also undertake loan "workout" activities without incurring owner/operator liability, provided the lender does not thereby "participate in management" as described above. Therefore, a lender can generally:
  - ▸ Restructure or renegotiate the terms of the security interest; and
  - ▸ Provide financial or other advice to the borrower.
- After foreclosure, a lender who did not "participate in management" prior to foreclosure can generally:
  - ▸ Maintain business activities;
  - ▸ Wind up operations; and
  - ▸ Take actions to preserve, protect, or prepare the property for sale;

  provided that the lender attempts to sell, re-lease property held pursuant to a lease financing transaction, or otherwise divest itself of the property in a reasonably expeditious manner using commercially reasonable means. This test will generally be met if the lender, within 12 months after foreclosure, lists the property with a broker or advertises it for sale in an appropriate publication.
- Regardless of CERCLA's security interest exemption from owner/operator liability, a lender may incur CERCLA liability as a generator or transporter if it meets the requirements of Section 107(a)(3) or (4) of CERCLA, 42 U.S.C. § 9607(a)(3) or (4), respectively.

Answers to Common Questions About the Effect of CERCLA on Lenders

Will EPA initiate a CERCLA enforcement action against a lender that performs a cleanup of contaminated property?

Under the Lender Policy, a lender may take a response action under Section 107(d)(1) of CERCLA, 42 U.S.C. § 9607(d)(1), or under the direction of an on-scene coordinator appointed under the National Contingency Plan (NCP, 40 C.F.R. Part 300), without being considered an owner or operator under CERCLA. Often referred to as the "Good Samaritan" provision, Section 107(d)(1) of CERCLA protects persons from liability related to actions taken or omitted while rendering care, assistance, or advice in accordance with the NCP with respect to the release of a hazardous substance that creates a danger to public health or welfare or the environment.

Will EPA initiate a CERCLA enforcement action against a lender that forecloses on a CERCLA facility and then leases that facility to another person?

Under the Lender Policy, a lender may foreclose on a CERCLA facility and then re-lease the facility if it was held pursuant to a lease financing transaction. Examples of lease financing transactions include national bank lease financing, leveraged leases, and single-investor leases. In these transactions, the lessor does not initially select the leased property, but acquires title to the property for and at the direction of the lessee. The lessor then recovers its loan (i.e., the purchase price of the property) through rental payments from the lessee and, in some cases, from the sale of the property to the lessee or another party at the end of the lease. Thus, the lessee is the borrower and the lessor is the holder of a security interest in the property. Re-leasing the facility following foreclosure in this type of arrangement is permissible under the Lender Policy because it indicates that the lessor is primarily protecting its security interest in the property.

Under the Lender Policy, a lender in an arrangement other than a lease financing transaction is generally not protected by the security interest exemption if it leases or re-leases the CERCLA facility after foreclosure. Such activities would indicate that the lender is neither holding evidence of ownership in the facility primarily to protect its security interest nor attempting to divest itself of the facility in a reasonably expeditious manner.

Can a lender be held liable under CERCLA to potentially responsible parties and other non-federal entities?

The Lender Policy describes internal policies and procedures to be used by EPA and DOJ personnel and does not create enforceable rights. As a result, courts may or may not follow the Lender Policy. However, recent judicial opinions indicate that a court facing lender liability issues is likely to apply principles and rationale that are consistent with EPA and DOJ's Lender Policy. See, e.g., United States v. Wallace, 893 F. Supp. 627 (N.D. Tex. 1995); Z & Z Leasing, Inc. v. Graying Reel, Inc., 873 F. Supp. 51 (E.D. Mich. 1995); Kemp Industries, Inc. v. Safety Light Corp., 857 F. Supp. 373 (D.N.J. 1994).

Will private parties that purchase contaminated property from lenders also be exempt from CERCLA liability?

No. Nothing in CERCLA exempts non-governmental parties from liability after they knowingly purchase contaminated property. However, EPA encourages prospective purchasers of contaminated property to contact their state environmental agencies to discuss these properties on a site-by-site basis. At sites where an EPA action has been taken, is ongoing, or is anticipated to be undertaken, various tools, including federal "prospective purchaser agreements," may be available to help prospective purchasers avoid liability related to contamination existing at the time of purchase.

Does the Lender Policy apply to state cleanup enforcement actions?

No. As noted above, the Lender Policy describes internal policies and procedures to be used by EPA and DOJ personnel and does not create enforceable rights. Consequently, neither state environmental agencies nor courts interpreting hazardous waste liability provisions under state law are required to apply the Lender Policy.

For Further Information

The Lender Policy was published in the Federal Register in Vol. 60, No. 237, at pp. 63517 to 63519 (December 11, 1995).

You may order copies of the Lender Policy from the National Technical Information Service (NTIS), U.S. Department of Commerce, 5285 Port Royal Rd., Springfield, VA 22161. Orders must reference NTIS accession number **PB95-234498**. For telephone orders or further information on placing an order, call NTIS at **703-487-4650** for regular service or **800-553-NTIS** for rush service. For orders via e-mail/Internet, send to the following address:

orders@ntis.fedworld.gov.

If you have questions about this fact sheet, contact Laura Bulatao in EPA's Office of Site Remediation Enforcement at (202) 564-6028.